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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1941.

No. 499.

MEMPHIS NATURAL GAS COMPANY,
Appellant,

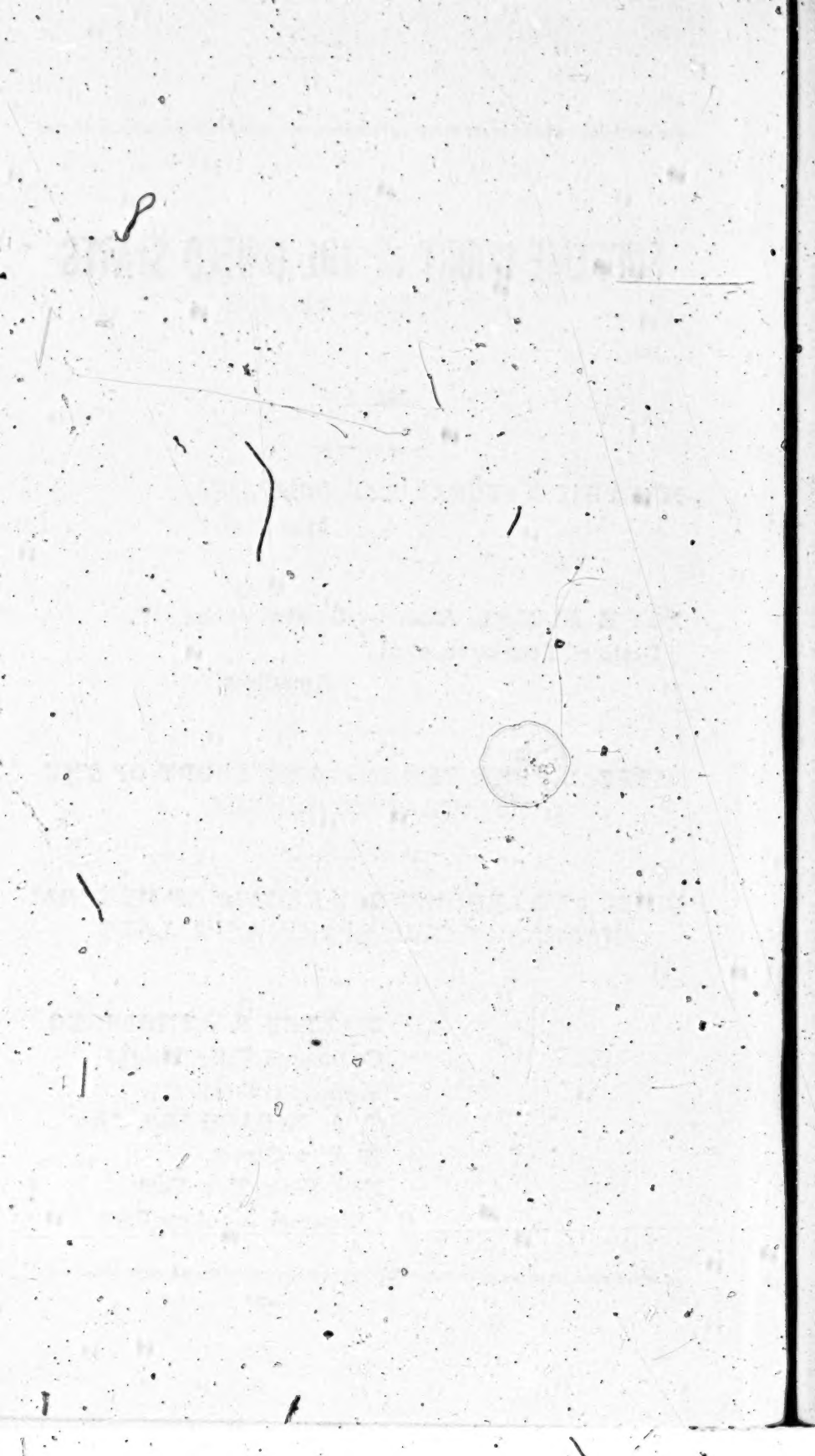
vs.

ROY H. BEELER, Attorney General of the State of Tennessee, et al.,
Appellees.

APPEAL FROM THE SUPREME COURT OF THE STATE OF TENNESSEE.

BRIEF AND ARGUMENT IN BEHALF OF MEMPHIS NATURAL GAS COMPANY, APPELLANT.

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OPINIONS DELIVERED IN THE COURTS BELOW.

No opinion delivered in either of the courts below has been officially reported and no one of the opinions has been published in any unofficial report. Therefore no reference is made either to any official or unofficial

report of these opinions. There are in the record five opinions delivered in the courts below.

(The Memorandum Opinion of Mr. Chief Justice Green of the Supreme Court of Tennessee, denying the Petition of Roy H. Beeler, Attorney General of the State of Tennessee, et al, for Supersedeas, and sustaining the jurisdiction of the Chancery Court of Davidson County, Tennessee to grant an injunction, is not in the record proper but is set out as Exhibit "B" to the Statement as to Jurisdiction, pp. 16-17.)

The first is the opinion of the Chancery Court of Davidson County, Tennessee, in which the cause originated. (Opinion of Chancery Court of Davidson County, Tennessee, R. 357-360; Statement as to Jurisdiction, pp. 13-16.)

The second is the Majority Opinion of the Supreme Court of Tennessee on Final Hearing, delivered by Mr. Special Justice Fancher. (R. 371-384; Statement as to Jurisdiction, pp. 17-32.)

The third is the Concurring Opinion of Mr. Justice McKinney, of Supreme Court of Tennessee, on Final Hearing. (R. 384-385; Statement as to Jurisdiction pp. 32-34.)

The fourth is the Dissenting Opinion of Mr. Justice Chambliss of Supreme Court of Tennessee on Final Hearing. (R. 385-389; Statement as to Jurisdiction pp. 34-37.)

The fifth is the Opinion of Supreme Court of Tennessee on Petition to Rehear, delivered by Mr. Special Justice Fancher. (R. 400-401; Statement as to Jurisdiction. pp. 38-40.)

STATEMENT OF GROUNDS ON WHICH JURISDICTION IS INVOKED

The purpose of this suit, which was instituted in the Chancery Court of Davidson County, Tennessee, against the Attorney General and the taxing authorities of the State of Tennessee, was to enjoin the enforcement against Memphis Natural Gas Company, appellant, of the excise statute of the State of Tennessee, on the ground that the appellant, a natural gas pipe line company, was solely engaged in transporting and selling natural gas in interstate commerce, and that the statute by its terms did not apply to the business of the appellant, and that if it were construed and held to apply to the business of appellant, then it was unconstitutional under Article I, Sec. 8, Clause 3, of the Constitution of the United States, in that it would attempt to impose a tax on the privilege of engaging in interstate commerce and would be an unwarranted burden on, regulation of, and interference with, interstate commerce. (Original Bill, R. 8-9.)

Thus there was drawn in question by appellant the validity of the statute, if construed so as to apply to the business of the appellant, on the grounds of its being repugnant to the Constitution of the United States and the provision thereof above set out.

It was further alleged that the application of the statute to the business of appellant would deprive it of a right, privilege and immunity guaranteed by the same constitutional provision.

The statutory provisions believed to sustain the jurisdiction of this court are Secs. 237 and 237(a) of the

Judicial Code, as amended by the Act of February 13, 1925, and the Act of January 31, 1928, as amended by the Act of April 26, 1928.

The statute thus challenged is found in Secs. 1316-1318 of the Official Code of Tennessee of 1932, and provides among other things that every corporation shall pay "annually an excise tax * * * equal to three per cent. of the net earnings" for its preceding fiscal year "arising from business done wholly within the state, excluding earnings arising from interstate commerce."

These sections of the Tennessee Official Code are set out in full in appellant's Statement as to Jurisdiction, (Statement as to Jurisdiction pp. 2-3) and for convenience are reprinted as Appendix "A" to this brief.

It is uniformly held by the Supreme Court of Tennessee that "the tax levied by this Act is a privilege tax upon domestic and foreign corporations *organized for profit and carrying on business in this State.* * * *Corporations not doing business in the State and those that derive no net earnings from business done in the State are not subject to the tax.*"[1] *Quicksafe Mfg. Corp. vs. Graham*, 161 Tenn. 46 at 48; *Bank of Commerce & Trust Co. vs. Senter*, 149 Tenn. 569.

The thing taxed being the privilege of doing business in the state, the statute is entirely unlike that involved in *Stone vs. Interstate Natural Gas Co.*, 103 Fed. (2d) 544 (C.C.A. 5th), affirmed 308 U. S. 522, where, in the language of the Circuit Court of Appeals, "the tax is laid on a domestic organization because of its mere

[1] Italics here and elsewhere supplied.

existence capitalized and ready to carry on its corporate activities. It need not do anything to incur it." (103 Fed. (2d) at 548.)

There was no question of the power of the Chancery Court to enjoin the enforcement of the statute against appellant, if either by its terms it did not apply to appellant or if constitutionally it could not be construed so to apply. (Opinion, Chief Justice Green, Statement as to Jurisdiction, pp. 16-17; Majority Opinion, Supreme Court of Tennessee, R. 371-384; Opinion, Supreme Court of Tennessee on Petition to Rehear, R. 400-401.)

The appellant in its Original Bill not only insisted that the statute properly construed did not apply to its business but that the construction or application of the statute so as to exact from it the excise tax would bring the Act under the inhibition of Article I, Sec. 8, Clause 3 of the Constitution of the United States, and would deprive appellant of a right, privilege and immunity guaranteed by the same provision of the Constitution of the United States. (R. 8.)

The Chancellor did not find it necessary to pass upon these constitutional questions, inasmuch as he held that the statute by its express terms did not apply so as to impose an excise tax upon appellant's business. (Opinion of Chancellor, R. 357-360.)

The appellant, having prevailed in the Chancery Court, was appellee in the Supreme Court of Tennessee, and in its brief in that court not only insisted that the Chancellor was correct in his holding as to the statute, but further insisted that any other construction or applica-

tion of the statute would render it invalid under Article I, Sec. 8, Clause 3 of the Constitution of the United States, and would deprive appellant of a right, privilege and immunity guaranteed by the same provision of the Constitution of the United States. (R. 369-370.)

Appellant, among other things in its brief, stated:

> "... it is our submission that any other construction or application of the statute to the transactions here involved different from that made by the Chancellor would immediately bring the statute as so construed and applied in conflict with the commerce clause of the Federal Constitution." (R. 369.)

And again:

> "Our insistence is that not only has the state expressly refrained from taxing interstate commerce, but that it does not possess the power to impose a tax upon the business in which the complainant was engaged in the years 1932 to 1935, and that if either this statute or any other statute had taxed the business of complainant during those years, as is now attempted to tax it, such a statute and its application would have been unconstitutional."
>
> (Appellant's Brief in the Supreme Court of Tennessee, R. 370.)

In this connection Article I, Sec. 8, Clause 3 of the Constitution of the United States was expressly relied upon.

The first time the statute was construed and applied so as to place this excise or privilege tax on appellant's interstate business was when the Majority Opinion was delivered by the Supreme Court of Tennessee. (Majority Opinion, Supreme Court of Tennessee, R. 371-384.)

The appellant immediately filed a Petition to Rehear, in which it asserted that this construction and application of the statute rendered it invalid and within the inhibition of Article I, Sec. 8, Clause 3 of the Constitution of the United States, conferring upon Congress the power to regulate interstate commerce. (R. 391-394.)

The Supreme Court of Tennessee, in its opinion overruling this petition, expressly recognized that the federal question had been made and stated that "obviously the claim of federally protected right was decided adversely to complainant." (Opinion of Supreme Court of Tennessee on Petition to Rehear, R. 400.)

Though their statement in regard to it is not entirely correct, appellees do in effect admit that the appellant properly drew into question the validity of the statute. That statement is: "The asserted invalidity of these code sections is based on what appellant conceives to be a conflict with the commerce clause of the Constitution of the United States. This contention was first made in the Supreme Court of Tennessee and was not seriously pressed there." (Appellees' Statement Opposing Jurisdiction and Motion to Dismiss the Appeal, p. 1.)

This statement is not entirely accurate because it is not correct to say that this contention was first made in the Supreme Court of Tennessee. It was made in the Chancery Court and was made in the Supreme Court of Tennessee both in the original and reply briefs of appellant and in its Petition to Rehear. Regardless of this, however, concededly it was properly made.

When as in this case a statute is fair on its face and yet is so construed and applied as to be counter to Article I, Sec. 8, Clause 3 of the Constitution of the United States, one who challenges this construction and application draws in question the validity of the statute, under Secs. 237 and 237(a) of the Judicial Code, as amended by the Act of February 13, 1925, and the cause may be removed to this Court by appeal (formerly by writ of error). *Merchants National Bank of Richmond vs. City of Richmond*, 256 U. S. 635.

This is necessarily true because no matter how fair a statute may be upon its face, the construction given it by the Supreme Court of the state is conclusive upon this Court and regardless of its wording the statute must be read with the gloss furnished by the opinions of the state supreme court.

In *Eureka Pipe Line Co. vs. Hallanan*, 257 U. S. 265, a West Virginia statute forbade the engaging in the business of transporting petroleum by pipe lines without the payment of tax of two cents per barrel. The Supreme Court of Appeals of West Virginia held that the statute applied to intrastate commerce, but nonetheless construed it as applying to oil which was produced in West Virginia and transported by the pipe line company without the state. It was urged upon this Court that inasmuch as the West Virginia court had held that the Act applied only to commerce within the state, there was no jurisdiction of writ of error "because there is (was) no question as to the validity of a statute so limited." It was further "argued that the mistake, if any, was not in approving the statute, but in the court's conception of interstate commerce."

This Court, however, in an opinion by Mr. Justice Holmes, rejected this argument and said:

> "But we must look at what the court has done, not at its mode of reaching the result. What it has done is to decide that the statute covers all the oil produced in West Virginia, and that it shall be upheld in so doing. The nature of the mistake that induced the act is immaterial. A case would not be withdrawn from the jurisdiction of this court in error by a declaration that a statute was addressed only to intrastate commerce if it was applied wholesale to freight passing across the continent. The fact that the error was less does not affect the principle involved. But, furthermore, the court only confined the statute to intrastate commerce 'as above defined;' that is, to commerce that embraced what the plaintiff carried on." (257 U. S. 265, at 270, 271.)

Mr. Justice Clarke, dissenting, was of the opinion that the remedy was by certiorari and not by writ of error and in this dissent as to jurisdiction Mr. Justice Brandeis joined. (257 U. S. 265, at 273-277.)

See also *United Fuel Gas Co. vs. Hallanan*, 257 U. S. 277.

On the same day on which the two last mentioned cases were decided, this Court reiterated its holding in an opinion by Mr. Justice Van Devanter in *Dahnke-Walker Milling Co. vs. Bondurant*, 257 U. S. 282, in which the Court of Appeals of Kentucky had applied a Kentucky statute, prescribing conditions on which corporations of other states might do business in that state, to a transaction which this Court found to be of an interstate character. The Court held that regardless of the wording

of the statute, when so applied the remedy was by writ of error (now appeal), and said:

> "Our conclusion on the jurisdictional question is that, as the state court applied and enforced to the plaintiff's disadvantage a state statute which the plaintiff seasonably insisted as so applied and enforced was repugnant to the Constitution and void, the case is rightly here on writ of error." (257 U. S. 282, at 290.)

Mr. Justice Brandeis and Mr. Justice Clarke dissented.

In addition to drawing in question the validity of the Tennessee statute, appellant expressly claimed that its right, privilege and immunity asserted under Article I, Sec. 8, Clause 3 of the Constitution of the United States, had been denied by the construction and application of the statute made by the Supreme Court of Tennessee. (R. 8, 369-370, 392, 394, 400.)

Under former practice this claim, if it alone had been asserted, would have furnished the basis for petition for certiorari. (Judicial Code, Secs. 237 and 237(b) as amended.)

Inasmuch as an appeal improvidently sought and allowed will now be treated as a petition for certiorari, at this stage of the case, "the objection," as Mr. Justice Holmes said in *Eureka Pipe Line Co. vs. Hallanan*, 257 U. S. 265, at page 270, "would be immaterial were we not required to determine upon which proceeding the decree should issue."

Secs. 237 and 237 (c) of the Judicial Code, as amended by Act of February 13, 1925, and Act of January 31, 1928, as amended by the Act of April 26, 1928.

Whether appellant is entitled to appeal because it drew in question the validity of the Tennessee statute as construed and applied by the Supreme Court of that state, its court of last resort, or whether it is entitled to a review by this Court as if it had filed a petition for certiorari because it also claimed a constitutional right and privilege under Article I, Sec. 8, Clause 3 of the Constitution of the United States, there can be no question as to the substantial nature of the Federal right involved.

Appellant insisted that its earnings, on which it was sought to levy the excise-privilege tax, were derived solely from interstate transportation and sale of gas, and that the only acts done in Tennessee in respect to the transportation and sale were maintaining the pipe lines, reducing the pressure of gas that it might be delivered, metering the amount delivered and related office work, and that these activities were entirely incidental to interstate commerce and that, therefore, they came within the protective rulings of *State Tax Commission of Mississippi vs. Interstate Natural Gas Co.*, 284 U. S. 41; *East Ohio Gas Co. vs. Tax Commission of Ohio*, 283 U. S. 465; *Ozark Pipe Line Corp. vs. Monier*, 266 U. S. 555; *Missouri, ex rel. Barrett vs. Kansas Natural Gas Co.*, 265 U. S. 298; *Penn. vs. W. Virginia*, 262 U. S. 553; *Eureka Pipe Line Co. vs. Hallanan*, 257 U. S. 265; *Public Utilities Commission of Kansas vs. Landon*, 249 U. S. 236.

In this connection appellant contended that in all instances its main pipe lines were tapped by the distributing companies which distributed the gas and by its one Tennessee consumer, and that in no case did it have any service lines or service the gas, and that therefore its activities did not fall within the scope of the decision of

this Court in *Southern Natural Gas Corporation vs. Alabama*, 301 U. S. 148.

The Supreme Court of Tennessee intimated that the appellant did engage in intrastate business by servicing customers. (Majority Opinion of Supreme Court of Tennessee, R. 382-383.)

The Supreme Court of Tennessee further held that the appellant engaged in intrastate business because it found that appellant was engaged in some kind of joint enterprise or partnership undertaking with a local distributor, Memphis Power & Light Company. (Majority Opinion of Supreme Court of Tennessee, R. 373-381.) As we shall fully point out in our Statement of the Case and Argument, the record supports neither finding; therefore, the Supreme Court of Tennessee erred in construing and applying the statute so as to impose an excise-privilege tax upon appellant's earnings derived solely from interstate commerce, because the effect of this was to tax the appellant for the privilege of engaging in interstate commerce.

STATEMENT OF THE CASE.

Question Presented.

The question presented in this case is whether the excise-privilege tax provided for in the Tennessee statute heretofore quoted from, and set out in full as Appendix "A," can be imposed upon appellant's earnings for the years 1932-1935 inclusive. Appellant's submission is that these earnings are immune from this tax because they were derived solely from interstate commerce and the imposition of the tax upon them would result in taxing the privilege of engaging in interstate commerce.

Nature of Business from Which Appellant's Earnings Were Derived for Tax Years in Question.

During the years in question appellant's entire earnings were derived from the interstate transportation and sale of natural gas. (R. 118.)

The appellant, a Delaware corporation, was the owner and operator during these years of an interstate gas pipe line 369.86 miles in length, extending from the gas fields near Monroe, Louisiana, through the states of Arkansas, Mississippi and into and through part of the State of Tennessee. (R. 33-36; Exhibits "A" and "B" to Tes. Henry C. Wallace, R. 33, 460A, 36, 461.)

Appellant originally purchased the natural gas transported by its pipe line under a gas purchase contract from United Gas Pipe Line Company. The delivery of this gas was made to appellant at its compressor station near Monroe, Louisiana. (R. 34; Exhibit "A" to Tes. Henry C. Wallace, R. 33, 460A.)

This gas, by means of compressor or "booster" stations was transported in appellant's gas pipe line through the states of Louisiana, Arkansas, Mississippi and into Tennessee. During the years in question, however, no compressor or booster station was operated by appellant in the State of Tennessee. (R. 36, 37, 48-49, 87, 106, 157.)

At points along the pipe line outside the State of Tennessee three customers, public utility distributing companies (one in Louisiana, one in Arkansas and one in Mississippi), tapped the pipe line and received gas under gas purchase contracts. (R. 38, 69.)*

* The following statement in the Majority Opinion of the Supreme Court of Tennessee is inaccurate: "Complainant furnishes one buyer in Arkansas, the Arkansas Power and Light Company, and none in Mississippi." (Appellant's Statement as to Jurisdiction, R. 372.)

In Tennessee two purchasers, public utility distributing companies (in Shelby County, Tennessee, Memphis Power & Light Co., in points in Tennessee outside of Shelby County, West Tennessee Power & Light Company) tapped appellant's main pipe line system and received gas under purchase contracts which had been entered into in the State of New York. (R. 40, 102; Exhibits "A," "B," "C." Tes., Birger L. Johnson, R. 103, 509-540; 104, 540-550; 104, 550-565.)

Appellant's customers tapped its interstate main gas pipe line system at various points, known as "city gate meter or measuring stations." (R. 40, 41.) This gas moved in a continuous flow out of appellant's main pipe line into the pipe lines of the two Tennessee public utility distributing companies, which companies sold and delivered gas to their local customers. (R. 40, 41, 105-106, 108, 115-116, 157.)

At the time of the withdrawal of the gas for the purpose of, and necessarily incident to, its delivery appellant measured the gas by meter and its pressure was reduced in some instances to an average of 100 pounds per square inch. (R. 42, 43, 49, 50, 57, 107, 158.)

Most of the gas which Memphis Power & Light Company received from the appellant was received at what is known as the Brooks Avenue Station in Shelby County, Tennessee. After receipt, Memphis Power & Light Company transported the gas to its Kansas Street Station in Memphis, and thence part to its generating plant for consumption and the remainder to its customers. (R. 32, 54, 55, 76, 77, 95, 188.)

The natural gas which appellant's customers thus obtained by tapping appellant's main gas pipe line system was at all times in continuous flow; none of the gas came to rest in Tennessee. Appellant did not own or operate any tanks, reservoirs or storage equipment in Tennessee. The gas was not treated or processed in any way. Nothing was extracted from it and no other gas was mixed with it: (R. 41, 45, 51, 96, 107, 108, 126, 147, 156, 189.)

All of complainant's pipe lines in Tennessee were main pipe lines. There were 6.9 miles of 18 inch line, 59.47 miles of 10 inch, 39.5 miles of 8 inch, 11.52 miles of 6 inch, 5.17 miles of 4 inch, .7 miles of 3 inch. (R. 34, 35; Ex. "B" to Tes., Henry C. Wallace, R. 36, 461; 111.)

Exhibit "A" to the Testimony of Henry C. Wallace (R. 33, 460A) is a map showing appellant's pipe line system. This map should be read in connection with Exhibit "C" to the Testimony of the same witness (R. 55, 479), which is a schedule showing dates of installation of delivery stations in Tennessee.

During the years involved here there was in Shelby County, Tennessee (Memphis), one main delivery point at Brooks Avenue, the terminus of appellant's 18 inch pipe line. There were three other delivery points to Memphis Power & Light Company in Shelby County: Whitehaven, Holly Ford Road and Oakville. Each of these is a small community served by Memphis Power & Light Company, which took delivery of the gas at points adjacent to the communities served by tapping appellant's main pipe line to Jackson, Tennessee. (R. 55, 56.)

In West Tennessee outside of Shelby County deliveries were made during the years in question to West Tennessee Power & Light Company at the "City Gates" of the following municipalities:

In Tipton County—Covington.
In Lauderdale County—Henning and Ripley.
In Gibson County—Humboldt.
In Madison County—Jackson.

(R. 42, 55, 480.)

See Agreement between Memphis Natural Gas Company and West Tennessee Power & Light Company. (R. 104, 550.)

Complainant did not own or operate or maintain any service lines, service equipment or any instrumentality of any kind which was or could be used in the local distribution of natural gas in the State of Tennessee, and complainant did not have any ownership or control of natural gas received by its customers in Tennessee after it had passed the meter stations at the points of delivery and into the pipe lines of the public utility distributing companies. (R. 45, 46, 56, 77, 105, 106, 107, 115, 116.)

The described method of appellant's operation was the same in each of the tax years in question. (R. 33.)

Background of Appellant's Organization.

In 1927 and prior thereto there was no distribution of natural gas in the City of Memphis. Manufactured gas was generated and distributed by Memphis Power & Light Company for cooking, water heating and a limited number of other uses. In that year the Memphis Chamber of Commerce was approached by an Alabama lawyer who had conceived the idea that it was desirable to bring natural gas to Memphis from the gas fields in order to

substitute it for manufactured gas, and to extend the use of natural gas to uses beyond those which had been feasible for manufactured gas. (R. 150, 151, 152, 153.)

Representatives of the Chamber of Commerce began negotiations with Memphis Power & Light Company in an effort to effect some arrangement by which the latter company would undertake the distribution of natural gas. Memphis Power & Light Company strongly and continuously opposed this plan, taking the position that the distribution of natural gas would be an unprofitable venture for it. To overcome this opposition representatives of the Chamber of Commerce approached the municipal authorities of the City of Memphis for the purpose of obtaining their cooperation in the bringing of natural gas to Memphis. (R. 150-151, 152-153.)

The City indicated that if Memphis Power & Light Company continued to oppose the venture and to decline to distribute natural gas, it would grant a franchise to a new company for the distribution of natural gas in Memphis, in competition with the manufactured gas which was distributed by Memphis Power & Light Company, whose franchise was not exclusive. (R. 150, 151, 153.)

A 1928 Delaware charter was obtained by Memphis Natural Gas Company, which charter was filed in the State of Tennessee that year. (R. 155; Ex. "A" to Tes., Brantley, R. 205, 208.) The company was financed by the sale of bonds, preferred and common stock and actual transportation of gas began January 1, 1929. (R. 153-160.)

Faced with the threat of competition Memphis Power & Light Company capitulated and agreed to distribute natural gas, under the terms of a contract which will be hereinafter more fully referred to. (R. 150-153.)

Appellees have unsuccessfully contended throughout this litigation that Memphis Natural Gas Company was an integral part of the Electric Bond & Share Company system and that Memphis Power & Light Company was a component of the same system, and that therefore because of this relationship Memphis Natural Gas Company, notwithstanding the interstate character of its transportation of natural gas, was nonetheless doing intrastate business in Tennessee. In view of this contention we briefly relate the facts upon which this claim is based. (See Tes., Beerman, R. 231, et seq.)

National Power & Light Company owned the majority of the voting stock of Memphis Power & Light Company. Electric Bond & Share Company owned 46.59 of the voting stock of National Power & Light Company. Shortly after the contract was entered into between Memphis Natural Gas Company and Memphis Power & Light Company, National Power & Light Company received 25% of the stock of Memphis Natural Gas Company, a percentage which was later reduced to 16.3% as a result of the issuance of other stock by Memphis Natural Gas Company (R. 119, 191, 192, 199.) At one time O. H. Simonds, and at another H. C. Abell, and at another Walter P. Armstrong, were directors of both Memphis Natural Gas Company and Memphis Power & Light Company. At no time did a majority of the Board of Directors of Memphis Natural Gas Company consist of persons who had any business relation with the Elec-

tric Bond and Share Company or any of its affiliates. (R. 172, 175, 202.)

Not only did Memphis Power & Light Company oppose the formation of Memphis Natural Gas Company and introduction of natural gas in Memphis, but it expressly declined to participate in the financing of this company. (R. 123.)

At all times the dealings between Memphis Power & Light Company and Memphis Natural Gas Company were at arm's length and when the so-called contractual settlements between the two companies were being discussed, they became exceedingly acrimonious, and litigation was threatened. (R. 90, 91, 112, 113, 115, 142, 164.)

At no time did Memphis Power & Light Company, National Power & Light Company, Electric Bond & Share Company or any associate or affiliate of Electric Bond & Share Company, ever dominate or attempt to dominate Memphis Natural Gas Company. (R. 90, 115, 116, 118, 160, 161, 202.)

On the contrary 48% of the voting stock of Memphis Natural Gas Company was owned by Commonwealth Gas Corporation. Four of the seven members of the Board of Directors of Memphis Natural Gas Company were members of the Board of Directors of Commonwealth Gas Corporation. The policies of Memphis Natural Gas Company were subject to the controlling influence of Commonwealth Gas Corporation. There was a management contract between Memphis Natural Gas Company and Commonwealth Management and Engineering Company, a wholly owned subsidiary of Com-

monwealth Gas Corporation. This contract authorized Commonwealth Management and Engineering Company to contract among other things for the purchase on behalf of and in the name of Memphis Natural Gas Company of such labor, material, apparatus and supplies as Commonwealth Management and Engineering Company should deem necessary for the operation of the properties and business of Memphis Natural Gas Company. There was no connection of any kind between Electric Bond & Share Company, or any of its affiliates, and Commonwealth Gas Corporation. (R. 52, 62, 73, 100, 131, 132, 177; Ex. "D," Tes. Henry C. Wallace, R. 64, 480, 484.)

Thus it is apparent that neither Electric Bond & Share Company, nor any of its associated or affiliated companies, in any wise dominated or controlled Memphis Natural Gas Company. Memphis Natural Gas Company did purchase its gas in the field from one of the Bond and Share Company group, but when the contract was entered into it was not only entered into at arm's length but no one representing Memphis Natural Gas Company at that time knew that the producing company had any connection with Electric Bond & Share Company. Memphis Natural Gas Company's customers in Mississippi and in Arkansas were Electric Bond & Share Company's subsidiaries. (R. 154.)

Mississippi Power & Light Company at one time lent Memphis Natural Gas Company $200,000.00 and Arkansas Power & Light Company at one time lent Memphis Natural Gas Company $120,000.00. Each of these was a simple business transaction and was made because

the respective distributors, Arkansas Power & Light Company and Mississippi Power & Light Company wished to enter new fields and to have Memphis Natural Gas Company transport its gas in interstate commerce and deliver it at new points to these distributors. Memphis Natural Gas Company was not in position to finance these undertakings and hence the temporary loans, which have now been repaid. (R. 181, 182, 197, 198.)

No opinion rendered by the Supreme Court of Tennessee was based on the finding of any corporate integration. These facts are related, however, in anticipation that this claim, which has been consistently made by appellees, will be pressed in this Court.

Appellant's Tennessee Office.

From 1932 to 1935 Memphis Natural Gas Company maintained an office in Memphis, Tennessee, having about 350 to 400 square feet of office space and 12 employees, consisting of accountants, bookkeepers and clerks, and all of the business transacted in this office was incidental to the transportation and sale in interstate commerce of natural gas and consisted of taking care of the payroll of the laborers on the line, billing Memphis Power & Light Company, West Tennessee Power & Light Company, Louisiana Power & Light Company, Arkansas Power & Light Company and Mississippi Power & Light Company and other such incidental matters. (R. 44, 60, 61, 91, 92, 135, 136, 147, 148, 159.)

Contract by Which Memphis Natural Gas Company Sold Gas to Memphis Power & Light Company To Be Distributed by the Latter Company to Customers of Memphis Power & Light Company.

By the terms of this contract Memphis Natural Gas Company agreed to sell to Memphis Power & Light Company its requirements of natural gas for resale for a period of fifteen years, with a provision for a ten year extension if the gas supply continued available. (Exhibit "A," Tes. Birger L. Johnson, R. 103, 509.)

In order to equip itself for doing so, Memphis Natural Gas Company agreed to construct a pipe line with an initial capacity of 60,000,000 cubic feet daily, and susceptible of expansion. (*Ibid*, R. 510.)

Memphis Power & Light Company agreed to extend its line to the delivery point agreed upon and to adapt its distribution system to natural gas. (*Ibid*, R. 510-511.)

The gas delivered by Memphis Natural Gas Company was to be measured by meters installed by that company, with the right in Memphis Power & Light Company to install checking meters and to test Memphis Natural Gas Company's meters. Before the 15th of each month a statement was to be rendered by Memphis Natural Gas Company for the gas delivered the preceding month, which statement was to be binding unless excepted to within ten days. The schedule of prices depended upon the purpose for which Memphis Power & Light Company resold the gas. This was to be determined by an examination of the meters and books of Memphis Power & Light Company. At the end of each year there was to be an adjustment between the companies. (*Ibid*, R. 511-517.)

In arriving at the amount then owed by one company to the other, the following formula was to be applied:

Memphis Natural Gas Company was assumed to have made an initial investment of $7,300,000.00, to which was to be added any capital additions, subject to reduction, however, by the extent to which its facilities were used to supply customers other than Memphis Power & Light Company. From the gross receipts from gas sold Memphis Power & Light Company there were to be deducted maintenance and operating costs, reasonable charges for renewals and replacements, an amount necessary to amortize on a fifteen year sinking fund basis the investment of Memphis Natural Gas Company, excluding maintenance and renewals and replacements, the amount paid for taxes and 6% on its investment. The result was the net "surplus" or "deficit" of Memphis Natural Gas Company. (*Ibid*, R. 517-520.)

Memphis Power & Light Company was assumed to have made an initial investment of $6,300,000.00 to which was to be added additions to its natural gas distribution system. From its gross revenues from the sale of natural gas were to be deducted the cost of maintenance and operation of its natural gas department, reasonable charges for renewals and replacements, a sum sufficient to amortize *the additions*, excluding maintenance and renewals and replacements, upon a fifteen year, 6% sinking fund basis, the amount paid for taxes and 6% on its investment, arrived at as above stated. The balance was to be the net "surplus" or "deficit" of Memphis Power & Light Company. (*Ibid*, R. 520-522.)

The purpose of arriving at these net "surpluses" and "deficits" was to use them as a yardstick for adjustment of the schedule of prices to be paid for various classes of gas as set out in Article Sixth of the contract. That schedule of prices was tentative and when the net surpluses and deficits were arrived at there was to be a cash adjustment at that time and then a change in the schedule of prices so as to effect, so far as could be foreseen, an equal rate of return to each Company. (*Ibid*, R. 522.)

Subsequent to this adjustment of prices, if at any time the deficits of the two companies were made up and Memphis Power & Light Company obtained from its Gas Department a 7½% return on its investment, and Memphis Natural Gas Company "a reasonable return in view of the hazards of the undertaking." (*Ibid*, R. 523) for previous years, the probability of a future surplus beyond this was to be eliminated by a reduction of the charges of Memphis Natural Gas Company to Memphis Power & Light Company and reductions by Memphis Power & Light Company of the rates charged its customers, the consumers. (*ibid*, R. 522-524.)

The contract provided not for a division of profits and losses, but was solely an agreement whereby the amount to be paid for the gas delivered by the Seller, Memphis Natural Gas Company, to the Buyer, Memphis Power & Light Company, was to be fixed and adjusted according to the result reached by the application of the formulae set forth in Articles Ninth, Tenth and Eleventh. (*Ibid*, R. 517-524.) The determinative language of the contract itself clearly established that these formulae for the annual contractual statements (set forth in Articles Ninth, Tenth and Eleventh) were simply the norm or

yardstick whereby the base rates of Article Sixth were to be adjusted.

Article Sixth definitely referred to these formulae in the following words:

> "*Sixth*: Subject to adjustment in accordance with the provisions of Article Eleventh hereof, the Buyer shall pay the Seller monthly for gas purchased hereunder during the preceding calendar month at the following rates:"
>
> (Here follow the base rates subject to such adjustment.) (*Ibid*, R. 515-516.)

It is clear, therefore, that the items to be adjusted were the "rates" to be paid by Buyer, Memphis Power & Light Company, to Seller, Memphis Natural Gas Company, and that the rates so adjusted constituted the ultimate price paid for the gas delivered by Memphis Natural Gas Company in interstate commerce under the above mentioned contract. (*Ibid*, R. 509-540.)

OPINIONS OF SUPREME COURT OF TENNESSEE

Majority Opinion of Supreme Court of Tennessee.

Mr. Special Justice Fancher, who delivered the Majority Opinion of the Supreme Court of Tennessee, treated as inconsequential the fact that appellant had filed its charter in Tennessee and maintained in Tennessee an office, for neither of these facts is referred to by him. He also rejected the idea of any corporate integration between the appellant and Electric Bond & Share Company, by saying that: "There seems to be separate corporate entity, as was found by the Chancellor." (R. 380.)

It is not entirely clear from his opinion as to whether he thought that the business of the appellant was such as to bring it within the rule of *Southern Natural Gas Corp. vs. Alabama*, 301 U. S. 148.

He did say:

> "While the cases are unlike the instant one, we are justified in holding that though the gas has come into Tennessee in a movement that is interstate in character, yet when it is sold to consumers by distribution or upon orders on demand, considering all its activities, it is intra-state business. This is true though the gas so furnished is drawn from interstate mains. Southern Natural Gas Corporation vs. Alabama, 301 U. S. 148." (R. 382.)

However, after fully discussing *Southern Natural Gas Corp. vs. Alabama*, he contrasted it with the case at bar by saying:

> "The main difference in the above case on the facts, to the facts here, consists in the Seller providing the service lines to the Tennessee company, and the further fact that there was no association between Seller and Buyer as in the instant case. We regard the instant case a stronger one to support the tax because of this joint enterprise feature." (R. 383.)

In *Southern Natural Gas Corp. vs. Alabama*, of course, the fact that the Southern Natural Gas Corporation did supply service lines was a controlling feature of the case. Thus Mr. Special Justice Fancher himself distinguished that case from the case at bar.

The joint enterprise feature which he mentioned has no connection with *Southern Natural Gas Corp. vs. Ala-*

bama. It was on this basis, however, that Mr. Special Justice Fancher rested his opinion. Not only did he say that "the case, as we view it, largely turns upon the contract between these two companies, and with the City" (R. 373), but when his opinion is analyzed it is clearly apparent that what he held was that Memphis Natural Gas Company was engaged in a partnership undertaking or a joint enterprise with Memphis Power & Light Company, which was a local distributor, and for this reason was engaged in intrastate business within the State of Tennessee.

Although this was his conclusion the only fact on which he relied was his construction of the contract, which he found to be a profit sharing arrangement. He concluded, therefore, as a matter of law that this profit sharing arrangement made the two companies joint entrepreneurs and therefore characterized the business of Memphis Natural Gas Company as intrastate business. (Majority Opinion of Supreme Court of Tenn., R. 371-383.)

Concurring Opinion of Mr. Justice McKinney.

Mr. Justice McKinney specially concurred but rested his opinion entirely upon the rule of *Southern Natural Gas Corp. vs. Alabama.* (R. 384-385.)

He concluded from the record that Memphis Natural Gas Company was engaged in servicing Tennessee customers and that this was determinative. In one respect his statement as to the record is incorrect, at least in its implications. He said that "in the instant cause, complainant piped the gas from Louisiana to Memphis, where, under one contract, a portion of it was turned

into a smaller pipe and delivered to the municipality for consumption at its electric generating plant." (R. 385.)

If by this statement was meant that Memphis Natural Gas Company ran a smaller pipe from its main line to the generating plant of Memphis Power & Light Company in order to supply that company with gas for consumption, it is incorrect. Memphis Natural Gas Company ran no pipe line from its main line to the generating plant of Memphis Power & Light Company. Memphis Power & Light Company tapped Memphis Natural Gas Company's main line at Brooks Avenue and from that point and via its Kansas Street station, Memphis Power & Light Company carried the gas to its generating plant, where it was consumed. (R. 188.)

This aside, however, Mr. Justice McKinney apparently found distribution in the fact that the main pipe lines of Memphis Natural Gas Company varied in their dimensions. The soundness of this finding we shall discuss in our argument. (Concurring Opinion of Mr. Jutice McKinney, R. 384-385.)

Dissenting Opinion of Mr. Justice Chambliss.

Mr. Justice Chambliss found "these Companies conceded to be legally distinct corporate entities." (R. 386.) He was of opinion that the contract between Memphis Power & Light Company and Memphis Natural Gas Company was in no sense a joint enterprise but a mere yardstick for determining the cost of gas.

He further found that the case was not ruled by *Southern Natural Gas Corp. vs. Alabama*, because "the 'distinction between the transportation of gas into a State

and the furnishing of gas to consumers within the State,' to quote the Alabama opinion, appears to have been preserved,—as it was not in that case." (R. 388.)

Opinion of Supreme Court of Tennessee On Petition To Rehear.

This opinion was concerned chiefly with making clear that the court has passed upon the constitutional question involved and explaining why no distinction was made between the gas delivered to West Tennessee Power & Light Company, with which concededly there was no joint undertaking, and that delivered to Memphis Power & Light Company. Mr. Justice Chambliss adhered to his dissent. (Opinion of Supreme Court of Tennessee on Petition to Rehear, R. 400-401.)

SPECIFICATION OF ASSIGNED ERRORS INTENDED TO BE URGED.

I.

Sections 1316, 1317 and 1318 of the Official Code of Tennessee of 1932 as construed and applied by the Supreme Court of Tennessee in this case are unconstitutional and in violation of Article I, Sec. 8, Clause 3, of the Constitution of the United States, in that as construed and applied by said court they exact of appellant an excise-privilege tax for the privilege of engaging in interstate commerce. This is I of appellant's Assignment of Errors accompanying Petition for Appeal to this Court. (R. 405-407.)

II.

In construing and applying Sections 1316, 1317 and 1318 of the Official Code of Tennessee of 1932, so as to exact an excise-privilege tax from the earnings of appel-

lant derived exclusively from interstate commerce, the Supreme Court of Tennessee deprived appellant of a right, privilege and immunity specially set up and claimed by it under the Constitution of the United States, said right, privilege and immunity being claimed under Article I, Sec. 8, Clause 3 of the Constitution of the United States, which delegates to Congress exclusive control of interstate commerce and prevents interference by a state with said interstate commerce by the imposition of a privilege tax or other direct burden on same. This is II of appellant's Assignment of Errors accompanying Petition for Appeal to this Court. (R. 407.)

III.

The Supreme Court of Tennessee erred in holding that under the contract between Memphis Natural Gas Company and Memphis Power & Light Company there was a joint enterprise or joint undertaking which took the business of Memphis Natural Gas Company in selling and transporting natural gas through its pipe line without the category of interstate commerce and stamped said sale and transportation by appellant with the characteristics of business done wholly within the state. This holding results in subjecting commerce that is wholly interstate to the excise-privilege tax imposed by Sections 1316, 1317 and 1318 of the Official Code of Tennessee of 1932, and in exacting of appellant a privilege tax for engaging in interstate commerce, in violation of Article I, Section 8, Clause 3 of the Constitution of the United States. This is III of appellant's Assignment of Errors accompanying Petition for Appeal to this Court. (R. 407-408.)

SUMMARY OF ARGUMENT.

The tax sought to be exacted of appellant has been definitively determined by the Supreme Court of Tennessee to be a privilege tax imposed on the actual doing of business within the State of Tennessee. (*Nature of Tax, infra*, p. 33.)

The business actually done by appellant was the interstate transportation of natural gas from the Louisiana fields through Arkansas, Mississippi and into Tennessee, where natural gas was sold to two public utility distributing companies and delivery made from the main pipe line system of appellant to the distribution systems of the utility customers. No distribution activity of any kind was carried on by appellant. All activities of appellant in Tennessee were incidental to the interstate transportation and sale of natural gas. All of the earnings of appellant in Tennessee were derived from such interstate transportation and sale.

It is the settled doctrine of this Court that under Article I, Section 8, Clause 3 of the Constitution of the United States a tax such as the Tennessee privilege tax cannot be imposed upon the business of a natural gas pipe line company whose activities are exclusively interstate. (*Appellant's Business During Tax Years Wholly Interstate and Not Subject to Tennessee Privilege Tax, infra*, p. 35.)

There is no merit in contentions, based upon considerations other than the method employed by appellant in transporting and delivering natural gas, urged to subject appellant to the tax:

(a) The contention that appellant's filing of its charter and maintaining an office in Tennessee subject it to the tax is without merit. (*Infra*, p. 47.)

(b) The contention that appellant and Memphis Power & Light Company were both members of the Electric Bond & Share Company system, and since concededly Memphis Power & Light Company was engaged in intrastate distribution of natural gas, therefore appellant was likewise, is without merit. (*Infra*, p. 52.)

(c) The contention that appellant must be construed as engaged in intrastate distribution of natural gas by reason of its contractual relationship with Memphis Power & Light Company, which is argued to have created, in effect, a joint enterprise, is without merit.

The contract was not a profit sharing arrangement but an arrangement for measuring prices charged by Memphis Natural Gas Company to the Memphis Power & Light Company and rates to be charged by Memphis Power & Light Company to its consumers.

Even if it had been a profit sharing arrangement, it could not have constituted the doing of business within the state of Tennessee by appellant.
(*Infra*, p. 54, et seq.)

(d) The contention that appellant might be constitutionally subjected to the tax imposed, even if it was engaged exclusively in interstate commerce, is without merit. (*Infra*, p. 65.)

ARGUMENT.

Nature of Tax.

The nature of the tax involved in this case is not a debatable question. It is a privilege tax. The privilege taxed is the doing of business in Tennessee. The Supreme Court of Tennessee has definitively decided both of these questions.

"Taxation of the privilege is upon the occupation or activity carried on amid the social, economic and industrial environment under protection of the state." • • • "The act imposes an excise tax, that is, a privilege tax, upon a class that embraces all domestic and foreign corporations or joint stock associations organized for profit and carrying on business within the State." • • • "Corporations or associations not doing business in the State and those that derive no net earnings from business are not subject to the tax whether they be foreign or domestic corporations." *Bank of Commerce & Trust Company vs. Senter*, 149 Tenn. 569, at 577 • • • 585.

The foregoing quotations clearly point out that the privilege taxed is the *doing* of business within the state and not the right or qualification to do business within the state. They also make it perfectly clear that the tax is not collectible from corporations "that derive no net earnings" from business within the state "whether they be foreign or domestic corporations."

In *Quicksafe Mfg. Corp. vs. Graham*, 161 Tenn. 46, a domesticated Delaware corporation, which succeeded a Tennessee corporation, was the owner of a patent right. It maintained an office in Tennessee, where it received

from a manufacturer royalties on machines manufactured in Connecticut and from there distributed. The Supreme Court of Tennessee, in holding that the corporation was not subject to the tax here involved, said:

> "The tax levied by this Act is *a privilege tax upon domestic and foreign corporations organized for profit and carrying on business in this state.*" (161 Tenn. 46, at 48.)

In the case at bar the Chancellor in his opinion lucidly pointed out the distinction between the authority to engage in business in Tennessee and actual doing of business, saying:

> "Many corporations have charters filed in the state of Tennessee under which they may be authorized to engage in a certain character of business, but do not do so, and the tax in this case is based upon the business *done* in the state of Tennessee as a matter of fact."
>
> (Opinion of Chancellor R. B. C. Howell, of Chancery Court of Davidson County, Tenn., R. 359-360. Emphasis as in opinion.)

This opinion thus sharply challenged the attention of the Supreme Court of Tennessee to the nature of the tax as defined by the lower court.

Moreover, the Supreme Court of Tennessee had before it the opinion of Assistant Attorney General Edwin F. Hunt, of Tennessee, which clearly defined the nature of the tax, in holding that the appellant was not liable for it:

> "The question does not arise as to whether the state could have included earnings from interstate commerce in the measure of the tax. Indeed such earnings may have been included under the constitu-

tion of the United States in the measure of tax of domestic corporations or of foreign corporations doing an intrastate business. However, since our statute explicitly excludes earnings arising from interstate commerce the only inquiry is whether the earnings of the Memphis Natural Gas Company in this State result from interstate commerce."

(Opinion, Assistant Attorney General, Edwin F. Hunt, Ex. "E," to Tes. Birger L. Johnson, R. 114, 575.)

The Supreme Court of Tennessee, by its silence in this case, accepted this definition as to the nature of the tax, as indeed it was necessary for it to do unless it desired expressly to overrule its prior decisions.

The nature of the tax being so clearly delineated, the issue here becomes sharply defined: Was appellant's busines during the tax years wholly interstate? If it was wholly interstate, can the tax imposed by the statute be collected for the privilege of doing this interstate business?

Appellant's Business During Tax Years Wholly Interstate and Not Subject to Tennessee Privilege Tax.

The record shows that all of appellant's earnings for the tax years were derived from its business of transporting natural gas and selling it at wholesale. If this business was wholly an interstate business, it follows that all of appellant's earnings were derived from an interstate business.

Appellant's operations during the tax years in question may be summarized:

It purchased natural gas in Louisiana; by means of its interstate pipe line it transported this gas through Louisiana, Arkansas, Mississippi and into Tennesee; under sales contracts which had been entered into in the state of New York this gas was delivered to appellant's two customers in Tennessee at City Gate Measuring Stations, pressure being reduced in order to effect delivery and the amount of gas delivered being metered; these two customers were public utility distributing companies. Appellant did not own or operate any local distributing pipe line; it had no control over the natural gas so transported after it left its main interstate gas pipe line and passed into the lines of the local public utility distributing companies. Appellant maintained an office in Memphis, Tennessee, wherein all the business done related exclusively to the operation and management of appellant's interstate pipe line operations in Arkansas, Louisiana, Mississippi and Tennessee. Memphis Power & Light Company received at the Memphis City Gate Meter Station from appellant's main gas pipe line gas in one bulk, part of which Memphis Power & Light Company conveyed in lines owned and controlled by it, to its generating plant for consumption, and part of which it used for local distribution to individual customers.

Delivery of comparatively small quantities of natural gas was made by appellant to Memphis Power & Light Company from appellant's main pipe line system, extending from Memphis to Jackson, Tennessee, at points in Shelby County, Tennessee, outside of the corporate limits of Memphis, from which points Memphis Power & Light Company served small communities in the county. Appellant made delivery from its main pipe line system

at seven City Gate stations outside of Shelby County, Tennessee, to West Tennessee Power & Light Company, for distribution by the latter company to as many municipalities located in West Tennessee.

In each instance of delivery appellant performed only such functions as were necessarily incidental to delivery and performed no distribution function whatsoever.

The operations thus summarized are identic with the operations of the Interstate Natural Gas Company in Mississippi, which were held, in the case of *State Tax Commission vs. Interstate Natural Gas Co.*, 284 U. S. 41, to be immune from the privilege tax which the State of Mississippi attempted to impose upon them. Mr. Justice Holmes in the opinion summarized the facts which were set out in an agreed statement:

> "The plaintiff has a trunk line of pipe extending from gas fields in Louisiana through Mississippi and back to Louisiana; 72.42 miles having a diameter of 22 inches, 8.11 miles having a diameter of 12 inches and 4.99 miles a diameter of 10 inches. It sells daily to distributors in Louisiana about 70,000,000 cubic feet of natural gas in summer and about 75,000,000 feet in winter. In Mississippi it sells as will be explained from 204,000 to 520,000 feet according to the season. The gas flows continuously from the gas fields in Louisiana and obviously, for much the greater part at least, in interstate commerce. But the appellants rely upon business done under two similar contracts made in New York to show that there was intrastate commerce in Mississippi that may be taxed without burdening the main activity that the State cannot touch.
>
> • • • •
>
> "Distributing companies tap the plaintiff's pipes near Natchez and the town of Woodville. *The gas*

withdrawn by the distributors is measured by a thermometer and a meter furnished by the plaintiff which is the only way in which it can be measured. The pressure of the gas is reduced by the plaintiff before it passes into the purchaser's hands. The work done by the plaintiff is done upon the flowing gas to help the delivery and seems to us plainly to be incident to the interstate commerce between Louisiana and Mississippi. The plaintiff simply transports the gas and delivers it wholesale not otherwise worked over than to make it ready for delivery to the independent parties that dispose of it by retail. (284 U. S. 41, at 43.)

It is to be noted that in the *Interstate case* there were present the same incidents of transportation of the gas that are here present—the measuring by a thermometer, the metering and the reduction of pressure. The record here shows that these are necessary incidents and that gas can not be transported in interstate commerce in any other way. (R. 50, 107.)

The *Interstate case* followed a long line of decisions by this Court which have established the principle that the transportation of oil or gas from one state to another is interstate commerce, and that it is beyond the power of a state to lay a tax on such interstate commerce in any form, whether on the transportation of subjects of commerce, or on the receipts derived therefrom, or the *occupation, or business, of carrying it on.*

East Ohio Gas Co. vs. Tax Commission, 283 U. S. 465;

Ozark Pipe Line Corp. vs. Monier, 266 U. S. 555;

Missouri, ex rel Barrett vs. Kansas Natural Gas Company, 265 U. S. 298;

Pennsylvania vs. West Virginia, 262 U. S. 553;

Eureka Pipe Line Company vs. Hallanan, 257 U. S. 265;
Public Utilities Commission of Kansas vs. Landon, 249 U. S. 236.

As was said by this Court in *Public Utilities Commission of Kansas vs. Landon*, 249 U. S. 236, "that the transportation of gas through pipe lines from one state to another is interstate commerce may not be doubted." (249 U. S. at 245.) The Court in that case fixed the time when this interstate commerce terminated when it said: "Interstate movement ended when the gas passed into local mains." (249 U. S. at 245.)

Applying this test to the case at bar, when the gas moved out of the main trunk pipe line of Memphis Natural Gas Company into the local distributing lines of Memphis Power & Light Company and of West Tennessee Power & Light Company at the various points of delivery located on appellant's main pipe line system the operation of Memphis Natural Gas Company and the business done in regard to the transportation and delivery of said gas was at an end. The interstate movement of the gas had terminated. Likewise the business and operation of the appellant had ceased.

There is no suggestion in the instant case that the appellant transported natural gas to the burner tips of any local consumer. The uncontradicted proof clearly shows that appellant did not own or operate any pipe lines, facilities, or instrumentalities of any character which were or could be used in connection with the distribution of gas to any local consumer in the State of Tennessee.

If such distribution activity had been carried on, admittedly there would have been intrastate commerce; for in *East Ohio Gas Co. vs. Tax Commission*, 283 U. S. 465, it was held that when a distributing company carried the gas to the burner tips of numerous household consumers this was an intrastate business notwithstanding the fact that the gas had come from without the state.

Southern Natural Gas Corporation vs. Alabama, 301 U. S. 148, is a case where, as to the business held subject to tax, this Court found present elements of local distribution. The contract between the gas corporation and the Tennessee Coal, Iron and Railroad Company provided for the establishment by the Gas Corporation of service lines and the record shows that such lines were established to handle distribution of the gas to various industrial plants of the purchasing company.

The Court, therefore, found that the situation was essentially similar to that which existed in *East Ohio Gas Co. vs. Tax Commission*, 283 U. S. 465, in which case East Ohio Gas Company maintained, owned and operated a municipal distribution system.

The decision is rested entirely upon the similarity between servicing many different plants by service lines and servicing many different individual consumers by means of a distribution system. So essentially was the gas company in the *Southern Natural Gas Corporation case* engaged in distribution that it not only delivered the gas by service line to many widely separated plants, but delivered it "at a pressure of not less than thirty pounds gauge at some mutually satisfactory location or

locations upon the premises of buyer." (301 U. S. 148, at 152.)

In the case at bar Memphis Natural Gas Company had not a single service line, it transported no gas to the premises of Memphis Power & Light Company or West Tennessee Power & Light Company, but these companies merely tapped the main pipe line system of Memphis Natural Gas Company.

Again we point out that the reduction of pressure made at the delivery points by Memphis Natural Gas Company was merely sufficient to enable delivery to be made into the lines of the distributing companies and was, therefore, entirely incidental to this delivery. This court did not overlook this fact in the *Southern Natural Gas Corporation case.* It pointed out that the servicing and distribution in that case distinguished it from *Ozark Pipe Line Corporation vs. Monier,* 266 U. S. 555, and *State Tax Commission vs. Interstate Natural Gas Company,* 284 U. S. 41, because in those two cases all things done within the state where the gas was delivered were, as in the case at bar, merely incidental to interstate commerce.

That the reduction of pressure in the case at bar was purely incidental to interstate commerce and only such as was necessary in order to effectuate delivery, is demonstrated by the fact that after Memphis Power & Light Company took possession and control of the gas, it was necessary for it still further and greatly to reduce its pressure before it could either use it or distribute it.

At Brooks Avenue Memphis Natural Gas Company delivered to Memphis Power & Light Company, in bulk,

almost all the gas bought by Memphis Power & Light Company. Only a small percentage for distribution by Memphis Power & Light Company to small Shelby County communities was delivered at other points where Memphis Power & Light Company tapped complainant's main pipe line system. Delivery at Brooks Avenue was made by Memphis Power & Light Company tapping at that point the main line of Memphis Natural Gas Company with one pipe. From the Brooks Avenue station Memphis Power & Light Company, in a pipe owned and controlled by it, took the gas to Kansas Avenue in Memphis. From that point Memphis Power & Light Company had branching pipes and in them carried some of the gas to its power plant where it was consumed as fuel, and the remainder of the gas was turned into channels for consumption by the public. Thus, according to the undisputed facts, Memphis Power & Light Company merely tapped the main line of Memphis Natural Gas Company and all separating, distributing and servicing was done by Memphis Power & Light Company.

The same was true at every other point where either Memphis Power & Light Company or West Tennessee Power & Light Company obtained gas. In each instance the main interstate pipe line system of Memphis Natural Gas Company was tapped and Memphis Natural Gas Company did nothing more than reduce the pressure and measure the gas incidental to its delivery.

In ascertaining whether or not a pipe line company is engaged in distributing gas the determinative test is not whether the gas is consumed by the one who receives it from the pipe line company but what is done by the pipe line company in the way of distribution. There might

be many ultimate consumers of the gas and yet no distribution by the pipe line company. On the other hand there might be one consumer of the gas which had many plants and still be distribution by the pipe line company. Mr. Justice McKinney, in his Concurring Opinion, comments upon the varying sizes of the pipe line. Not all of appellant's main line pipe lines were of the same size. The exact facts are shown by the Map, Exhibit "A" to the testimony of Henry C. Wallace, and by Exhibit "B" to the testimony of the same witness. (R. 35-36, 33, 460A; 36, 461.)

In each instance, however, these were main pipe lines and not one of them was or had any attribute of a service line. They were not used for distribution but as main lines. The pressure on them was not that of a service line but the pressure necessary to transport gas in a main pipe line, varying between 400 pounds and 100 pounds per inch, and never less than 100 pounds, for delivery to the Memphis City Gate. (R. 42, 49, 158.)

Distribution required further and drastic reduction of pressure by the distributing companies. It would have been impossible to permit the natural gas to travel through a distribution system at the high delivery pressures. (R. 50, 87, 125.)

Such an extreme reduction of pressure was necessarily made by Memphis Power & Light Company before the natural gas received by it from appellant was used by consumers that frequently when the gas jet was turned on in the home of the consumer, the pressure was as low as one-half pound per inch. (R. 156, 188.)

Nowhere in the *Southern Natural Gas Corporation case* does this Court mention as a basis for its decision the fact that the Tennessee company consumed the gas instead of distributing it. The characteristic of intrastate business was found in servicing and distribution and not in consumption by the Tennessee company.

We put an illustration:

An individual owns a large subdivision in one state. Title to all the dwelling houses in the subdivision are in him and under his contract with his tenants he agrees to furnish them natural gas for heating the houses. This natural gas is brought to the subdivision from another state in interstate commerce. If the owner of the subdivision taps the main pipe line and distributes the gas to his tenants the pipe line company is engaged in interstate commerce. If the pipe line company not only transports the gas in interstate commerce, but runs service lines through the streets of the subdivision to each house and thus services the gas, this is intrastate commerce.

The distinction is perfectly apparent. It rests not upon whether the purchaser is the consumer, but upon whether the transporter is the distributor. The distinction between transportation and distribution of gas is well recognized and these terms have a well defined meaning.

Mr. Justice Butler, in *East Ohio Gas Co. vs. Tax Commission of Ohio,* supra, accurately described what constitutes distribution of gas when he said:

> "But when the gas passes from the distribution lines into the supply mains, it necessarily is relieved of nearly all the pressure put upon it at the stations of the producing companies, its volume thereby is expanded to many times what it was while in the

high pressure interstate transmission lines, and it is divided into the many thousand relatively tiny streams that enter the small service lines connecting such mains with the pipes on the consumers' premises. So segregated the gas in such service lines and pipes remains in readiness or moves forward to serve as needed. The treatment and division of the large compressed volume of gas is like the breaking of an original package, after shipment in interstate commerce, in order that its contents may be treated, prepared for sale and sold at retail."

(283 U. S. 465, at 470, 471.)

In the case at bar, however, Memphis Natural Gas Company had absolutely nothing to do with the gas after it left its "high pressure interstate transmission lines." Appellant did not divide the gas "into the many thousand relatively tiny streams that enter the small service lines connecting such mains with the pipes on the consumers' premises," nor did appellant subdivide the gas so that it might enter the service line that led to Memphis Power & Light Company power plant, there to be consumed as fuel. Memphis Natural Gas Company delivered only the "original package" at the Brooks Avenue station and elsewhere. These packages were broken and distributed not by appellant, but by Memphis Power & Light Company and West Tennessee Power & Light Company. It is entirely fallacious to insist that the mere fact that any commodity passing in interstate commerce is consumed by the one to whom it is delivered instead of being resold in any respect alters the interstate nature of the delivery.

Cf. *Brennan vs. City of Titusville*, 153 U. S. 289;
Best & Company, Inc., vs. A. J. Maxwell, 311 U. S. 454.

In analyzing the opinions of the Supreme Court of Tennessee we have already pointed out that Mr. Special Justice Fancher did say without specification that when "it (the gas) is sold to consumers by distribution or upon orders on demand, considering all its activities, it is intrastate business" (R. 382), adding however that the distinction between the instant case and the Southern Natural Gas Corporation was that in the case at bar there were no service lines as there were to the Tennessee company. He thus leaves uncertain wherein he found distribution.

Mr. Justice McKinney, in his concurring opinion, is at least more specific, for he found distribution in the fact that the main pipe lines of Memphis Natural Gas Company in the State of Tennessee varied in their diameter, apparently being of opinion that this converted them into service lines.

We fail to follow this reasoning, especially in view of *State Tax Commission vs. Interstate Natural Gas Company*, 284 U. S. 41, a case where interstate transportation was carried on in pipe lines with diameters of 22, 12 and 10 inches, respectively. It is entirely immaterial that there should be a variance in the sizes of the pipe lines as long as they are main pipe lines and not service or distribution lines. Function of the pipe lines, not size, is the criterion. Appellant's pipe lines, regardless of size, were all main transportation lines, not distribution or service lines.

Our submission therefore is that in delivering and transporting this gas, Memphis Natural Gas Company was engaged in interstate commerce and that all things

done in connection therewith, such as maintaining the pipe lines, metering the gas and reducing the pressure, were done purely as incidents to this interstate commerce. That this was the true situation as reflected by the record is clearly set out in the Dissenting Opinion of Mr. Justice Chambliss. (R. 385-389.)

The entire earnings on which it is sought to lay the excise-privilege tax were derived from this interstate transportation and sale.

It is apparent therefore that if any intrastate business is to be found, it must be found in something other than the method of transporting and delivering the gas. The attempt is made to find it in the fact that appellant maintained an office in Tennessee.

Claim That Appellant's Filing of Its Charter and Maintaining an Office in Tennessee Subject It to the Tax.

None of the opinions of the Supreme Court of Tennessee was specifically based upon the fact that appellant had filed its charter and did maintain an office in Tennessee during the tax years in question, although this fact was mentioned by the Majority Opinion. (Majority Opinion, Supreme Court of Tennessee, R. 372-373.)

The testimony shows without dispute that during the tax years in question neither the Memphis office nor the company, itself, transacted any business whatever except that which related to the transportation of gas in interstate commerce. Moreover, during these years its entire income was derived from the aggregate amounts paid under their contracts by Louisiana Power & Light Com-

pany, Arkansas Power & Light Company, Mississippi Power & Light Company, Memphis Power & Light Company and West Tennessee Power & Light Company.

The Chancellor found:

> "The complainant maintains an office in Memphis, Tennessee, and the business transacted at this office during the years in question was exclusively the operation and management of the company's pipe line referred to." (R. 359.)

There did exist in Tennessee a tax or fee for the filing of appellant's charter in Tennessee and that tax was paid initially and annually after the filing of the charter. It was $150.00 per year. (R. 204.)

This Court has never held—as far as we can find—that the mere filing of a charter in a state and the maintaining of an office in that state purely incidental to the transaction of interstate business by a foreign corporation amounted to the doing of an intrastate business. *Ozark Pipe Line Company v. Monier*, 266 U. S. 555, is precisely to the opposite effect. The Court found "nor is it material that appellant applied for and received a Missouri license or that it had the power thereunder to exercise the right of eminent domain." (266 U. S. 555, at 567.)

That case in discussing the maintenance of a Missouri office by the pipe line company reaffirmed the rule adopted in *Heyman vs. Hays*, 236 U. S. 178, which involved facts closely paralleling what was done by the Tennessee office of Memphis Natural Gas Company.

The *Ozark Pipe Line case* was approved in *Anglo-Chilean Nitrate Sales Corporation vs. Alabama*, 288 U. S. 218. There the corporation had filed its charter in Alabama and thus become authorized to do business in that state, but had actually transacted only interstate business. This Court found the authorization not to amount to intrastate business, supporting the imposition of a franchise tax, saying, "The fact that appellant qualified to do business in Alabama was not, and rightfully can not be, held to sustain the tax." (288 U. S. 218, at 224.)

Nothing is found in the opinion in *Southern Natural Gas Corporation vs. Alabama*, 301 U. S. 148, which in any wise impinges upon the authority of *Ozark Pipe Line Company vs. Monier, supra.*

The Court in the *Southern Natural Gas Corporation case* did comment upon the fact that the gas company did have an Alabama office. The discussion immediately followed the determination of the Court as to the nature of the statute, which determination concluded with the following sentence: "By compliance with the statute appellant obtained the privilege of engaging within the State in any of the activities which its charter authorized." (301 U. S. 148, at 153.) Immediately thereafter, as if to point out that the gas company had to some extent at least availed itself of this privilege, followed the statement as to the maintenance of an office in Alabama.

That the Court found significant the maintenance of this office primarily as it related to the kind of tax involved in that case is we think demonstrated by the fact that *Stone vs. Interstate Natural Gas Co.*, 103 Fed. (2d) 544 (C.C.A. 5th) Aff'd, 308 U. S. 522, which involved a

case where it was held this kind of tax was enforceable notwithstanding the fact that the business of the gas company was concededly interstate, was affirmed on the authority of the *Southern Natural Gas Corporation case.*

When Mr. Chief Justice Hughes, in the *Southern Natural Gas Corporation case,* did come to discuss *Ozark Pipe Line Company vs. Monier,* he distinguished it from the case he was deciding on the ground that "nothing was done in Missouri except in furtherance of transportation. Oil was neither received nor delivered in that State. The business actually carried on 'was exclusively in interstate commerce' and whatever was done within Missouri in maintenance of an office or otherwise was 'all exclusively in furtherance of its interstate business.'" (301 U. S. 148, at 155.)

The effect of this, of course, was to reaffirm the authority of *Ozark Pipe Line Company vs. Monier.* So far as the maintenance of the Alabama office was in the *Southern Natural Gas Corporation case* related to intrastate business, it did not effect a metamorphosis by which interstate business became intrastate business, but merely increased the amount of intrastate business which was created by the distribution. In that case the distribution of natural gas was the foundation of intrastate business and the office business *which related to that local distribution* was merely the super structure on that foundation.

The situation is greatly clarified by the dissenting opinion of Mr. Justice Cardozo in *Anglo-Chilean Nitrate Sales Corp. vs. Alabama,* 288 U. S. 218. Mr. Justice Car-

dozo dissented in that case on the ground that the Alabama courts had already held (as this Court in the *Southern Natural Gas case* found they had later held) the statute in question to impose a tax on the privilege of doing business in Alabama, regardless of whether business was done. Being of this opinion he had this to say about the fact that in *Ozark Pipe Line Company vs. Monier, supra,* the gas company filed its charter in Missouri and there maintained an office:

> "This, however, was the very business that was incidental to the federal right. The privilege to transport upon the interstate journey was an essential incident of commerce, and so an emanation from the federal power. The court did not hold that the tax would have been unlawful if laid upon a franchise emanating from the power of the state."
>
> (288 U. S. 218, at 236.)

Accepting this analysis it becomes manifest that in this case the privilege of interstate transportation of natural gas was "an emanation from the federal power," so all things incidental thereto were "an emanation from the federal power," including not only the reduction of pressure, metering, and maintenance of the pipe line, but maintenance of the Tennessee office.

The right to do a local business in Tennessee was "a franchise emanating from the power of the state." The tax, however, is not laid upon this franchise, and it is not here involved. Therefore the maintenance of the Tennessee office is not determinative one way or the other. If the appellant was engaged solely in the interstate transportation of natural gas, the work of that office was entirely incidental thereto. If on the other

hand appellant was engaged in distributing natural gas in Tennessee, then part of the work of the Tennessee office necessarily related to that distribution. If otherwise intrastate business was not done in Tennessee the maintenance of the Tennessee office does not alter this fact. If otherwise intrastate business was done in Tennessee, then the maintenance of the Tennessee office might increase that business because part of it would necessarily relate thereto.

Claim That Appellant Part of Integrated Electric Bond & Share Company System and Claim of Joint Enterprise.

Pressed both in the Chancery Court and in the Supreme Court of Tennessee by the appellees was the contention that Memphis Natural Gas Company was an integral part of Electric Bond & Share Company system and under its domination and control, and so, as it was insisted, was Memphis Power & Light Company. Therefore it was argued that inasmuch as Memphis Power & Light Company was concededly engaged in the local distribution of gas in Tennessee, Memphis Natural Gas Company as its *alter ego* was so engaged.

In connection with this insistence it was urged that in some instances, even though there was not the ownership of a majority of stock, there might be such inter-connection between two corporations that they became in effect a single entity. *United States vs. Union Pacific R. Co.*, 226 U. S. 61, a case where there was an ownership of 46% of the stock and actual domination under the facts, was relied on.

In the case at bar not only was there no testimony tending to show such domination but the uncontradicted evidence was to the contrary.

In our Statement of the Case (supra, p. 18) we have fully set out the facts, which show that there was no control of Memphis Natural Gas Company, Memphis Power & Light Company or Electric Bond & Share Company or any of its affiliates. We have also shown that in fact Memphis Natural Gas Company was dominated by Commonwealth Gas Corporation which had no connection of any kind with Electric Bond & Share Company or any one of its subsidiaries. It is unnecessary either to restate these facts or to argue them. This is true because both the Chancery Court and the Supreme Court of Tennessee affirmatively found against this contention.

The Chancellor in his opinion dealt with this insistence of the appellees in the following language:

> "It is also insisted by the defendants that the complainant company is an integral part of the Electric Bond and Share group of corporations and so interlocked with the corporation in Louisiana from which it purchases its gas, and the corporate purchasers from it in Tennessee, that they are component parts of the same enterprise and therefore liable for the tax. After a careful examination of all the proof and the entire record, the Court is of opinion that this contention of the defendants is not established. The Electric Bond and Share group of corporations do not dominate and control the complainant corporation and the complainant's dealings with the distributing companies has been by contract entered into after much discussion and some delay, which constitute these distributing corporations buyers of gas from the complainant company in the

ordinary course of trade, and not by reason of any dominating influence of a holding company."
(R. 360.)

Mr. Special Justice Fancher, in delivering the Majority Opinion of the Supreme Court of Tennessee, accepted this finding of the Chancellor:

> "There seems to be separate corporate entity, as was found by the Chancellor. This does not preclude a conclusion that these gas companies acted in concert and each was a party to and interested by contract in the operations, profits and/or losses of the other and that the whole business is so intertwined as to make their business joint."
> (R. 380.)

This contention being thus disallowed by the Tennessee courts, we pass to consideration of the basis upon which, as we have already pointed out, the Majority Opinion of the Supreme Court of Tennessee was primarily rested—that is, that when the contract between Memphis Natural Gas Company and Memphis Power & Light Company is considered "the whole business is so intertwined as to make the business joint." (R. 380.)

Though not abundantly clear, under careful scrutiny, however, it emerges that Mr. Special Justice Fancher was of opinion that the case "largely turns upon the contract between these two companies and with the City." (R. 373.)

In treating of this he held that the contract was a profit sharing contract and then assumed that if it was a profit sharing contract the effect of it was to convict Memphis Natural Gas Company of doing an intrastate business.

While he did in the course of his opinion refer to a joint undertaking, it is apparent from the connection in which this expression was used that he had always in mind profit sharing.

In regard to the inception of the arrangement, he stated that "these two corporations cooperated jointly in the scheme of bringing natural gas into Memphis and distributing it to the consuming public." (R. 373.)

The facts which we have set out (supra, p. 16) disclose that instead of there being any such joint undertaking in the beginning, what actually happened was that those who promoted Memphis Natural Gas Company conceived the idea of an interstate gas pipe line from the gas fields to Memphis, and with the aid of the City forced Memphis Power & Light Company to become a reluctant distributor of this gas. There was no common thought or common purpose between the two companies, but the entire idea was that of Memphis Natural Gas Company, and Memphis Power & Light Company became a distributor not because it desired to further that purpose but in order to escape the threat of competition.

The confusion of thought in the Majority Opinion which fails to distinguish between profit sharing and a joint enterprise is disclosed by the statement that "even without joint control of the operations that produce profits, persons or corporations may establish relationships that will result in a sharing of profits, each with the other. There is no law against two public utilities engaged in supplying gas to a community to so divide or parcel their work as to give each a separate manage-

ment of a portion and then pool their earnings, regardless of the technical rules of partnership. The right to contract is free enough to include such an arrangement, and there is no vice in it." (R. 374.)

And in another portion of the opinion it was said that: "The entire set-up and the whole contract between the two companies and the public shows a joint understanding." (R. 378.)

Naturally there was a joint understanding, otherwise there would have been no meeting of the minds and no contract. Again it is said that "in reality there was an operation in which both companies were jointly interested. There was an allotment of work performed but a division of the entire results of that work." (R. 379.)

The reading of the entire opinion will disclose what these quotations illustrate, that Mr. Special Justice Fancher believed that the contract amounted to the sharing of profits and assumed that if this was true, then necessarily Memphis Natural Gas Company was engaged in intrastate commerce because the Memphis Power & Light Company was so engaged. We shall endeavor to point out that neither the belief nor the assumption is justified.

The contract between Memphis Natural Gas Company and Memphis Power & Light Company was not a typical profit sharing arrangement nor was it, in the true sense of that term, a profit sharing contract. It was a sales contract with certain provisions for adjustments of the prices for which the commodity—natural gas—was sold. This is demonstrable by an examination of the contract.

Article Sixth began:

> "SIXTH. Subject to adjustment in accordance with the provisions of Article Eleventh hereof, the Buyer shall pay the Seller monthly for gas purchased hereunder during the preceding calendar month at the following rates:"
>
> (Ex. "A," Tes. Birger L. Johnson, R. 103, 515.)

The remainder of this article listed the charges made for the gas, these being dependent upon the uses to which the gas was put by Memphis Power & Light Company, with a catch-all provision covering unaccounted for gas. (*Ibid*, R. 515.)

Here, as elsewhere, the contract appropriately used the terms "Buyer" and "Seller" and referred to gas "purchased." The "adjustment" referred to was an adjustment of the sales prices.

Article Ninth provided for the furnishing of a statement by "the Seller"—Memphis Natural Gas Company—to "the Buyer"—Memphis Power & Light Company "and to the City of Memphis," the first paragraph of that article being:

> "NINTH. Within three months after the expiration of the first and each successive year after the date on which the Seller begins to deliver natural gas to the Buyer hereunder (each such first and successive year being herein sometimes referred to as a 'contract year'), the Seller shall deliver to the Buyer and to the City of Memphis, a statement setting forth in reasonable detail:" (*Ibid*, R. 517.)

This statement was to contain: (1) the amount of the Seller's investment which was arrived at by adding to

an agreed amount additional investments; (2) the gross revenues under the base prices of the Seller which consisted of the amount paid by the buyer to the Seller for natural gas; (3) costs to the Seller of maintaining and operating its pipe line; (4) amounts necessary for reserves for renewals and replacements or extraordinary maintenance not covered by (3); (5) amount necessary to amortize the Seller's investment; (6) taxes; (7) 6 per cent return on Seller's investment and (8) the net "surplus" or "deficit" of the Seller for the contract year, these to be arrived at by subtracting from the gross revenues (2) the aggregate of the amount provided for in (3), (4), (5), (6) and (7).

Article Tenth provided for a statement to be furnished by the Buyer "to the Seller and to the City of Memphis." This statement was not to be identical with the statement to be furnished by the Seller—Memphis Natural Gas Company, to the Buyer—Memphis Power & Light Company, but it was specifically provided that it should contain: (1) the Buyer's investment, arrived at by adding to an agreed initial amount *additions* to its natural gas distribution system; (2) gross revenues of the Buyer from the Seller of natural gas during the contract year; (3) cost of maintaining and operating its natural gas distribution system; (4) sums necessary to maintain reserves necessary for renewals, replacements or extraordinary maintenance; (5) amount necessary to amortize any additions to its original investment made by the Buyer for expanding its natural gas distribution system, but *not including any provision for the amortization*

of the Buyer's original investment for distribution[a]; (6) taxes; (7) 6 per cent return on the Buyer's investment and (8) "the net surplus or net deficit of the Buyer for such contract year as determined by subtracting from the gross revenues set out in (2) above, the sum of the amounts set out in (3), (4), (5), (6) and (7), above."
(*Ibid*, R. 522.)

These so-called net "surpluses" and net "deficits" which were later dealt with under Article Eleventh of the contract were not in the ordinary sense profits or losses, such as are distributed or liquidated under a partnership arrangement. They were amounts arrived at by definite artificial formulae agreed upon by the parties. Moreover, the "surpluses" or "deficits" of the "Seller" —Memphis Natural Gas Company—and of the "Buyer" —Memphis Power & Light Company were arrived at in distinct and differing ways. The purpose of this provision becomes apparent when Article Eleventh of the contract is considered. True, under this article the artificially created surpluses or deficits were to be divided between the parties, but this was merely the first step to the real re-arrangement or adjustment provided for by that article.

Not subsequent to this preliminary step, but "*at the same time*, the parties shall agree upon such adjustments, if any, in the rates set forth in Article Sixth hereof as may be calculated to be necessary in order as nearly as

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[a]In this respect the statements to be furnished by the Seller and by the Buyer are diametrically different. This is true notwithstanding the following statement in the Majority Opinion: "By the Tenth Article, Buyer was to deliver, yearly, to Seller and to the City of Memphis, the same information of its affairs and operations as those required of Seller, listed above." (R. 375.)

possible to effect an equal division of any contemplated combined surplus and/or deficit for the contract year then current and for subsequent contract years." (*Ibid*, R. 522.)

In other words, at the time the check passed the prices under Article Sixth were to be adjusted so that as far as possible the future passing of checks would be obviated.

The contract further provided that after the "deficits" of both parties were made up, that is after they had received repayment for all of the charges provided for in the contract and the 6 per cent return, and the Buyer—Memphis Power & Light Company—had received in addition 1½ per cent per annum, thus making its total return 7½ per cent per annum, the balance should be either paid to or retained by Memphis Natural Gas Company. This was to continue without any further changes of the prices set out in Article Sixth until Memphis Natural Gas Company had received, in addition to its 6 per cent on its investment "a reasonable return in view of the hazards of the undertaking."

When this balance exceeded an amount sufficient to compensate Memphis Natural Gas Company for the hazards of the undertaking the excess above this was to be used for the reduction of rates. This was to be done by reducing the prices provided for in Article Sixth by an amount comparable to the excess above the returns thus allowed to Memphis Power & Light Company and Memphis Natural Gas Company, that is, 7½ per cent to Memphis Power & Light Company and 6 per cent

plus an additional reasonable return to Memphis Natural Gas Company. This reduction of prices provided for under Article Sixth necessarily, of course, would have reduced the operating expenses of Memphis Power & Light Company because it would have reduced the aggregate amount that would be paid by that company for its gas. This reduction was to be passed on to the consumers by Memphis Power & Light Company by a rate reduction accorded them. This, of course, was the interest of the City in the contract. (*Ibid*, R. 522-524.)

This analysis of the contract, especially when set against the background and seen in the light of the conditions under which it was entered into, clearly shows its purpose. The parties to the contract were confronted with what to them was a novel situation. Memphis Natural Gas Company had never before engaged in transportation of natural gas. Memphis Power & Light Company had never distributed natural gas. The sale prices for natural gas were, therefore, necessarily experimental. Only by experience could it be determined what prices would be fair and reasonable to each company. The adjustments, therefore, were used as a yardstick to measure fair prices during the life of the contract because they were incapable of ascertainment at the time the contract was executed. This, and not any profit sharing, was the purpose of the provisions to which we have referred.

This view is, of course, strengthened by the attitude of the City toward, and its interest in, the contract. That interest was to secure natural gas for the citizens of Memphis at the lowest price commensurate with a fair

return to Memphis Natural Gas Company and Memphis Power & Light Company. This, too, was experimental and therefore these rates also were subject to adjustment should the return prove sufficient to permit of their reduction.

It, of course, will not be suggested that in respect to the prices to the consumer these provisions of the contract were anything more than a measuring rod. But if a measuring rod in regard to the rates to be charged the consumer, they were equally a measuring rod of prices to be charged by Memphis Natural Gas Company to Memphis Power & Light Company.

Entirely absent both from the record and from all opinions of the Supreme Court of Tennessee is any suggestion that there was any joint control by Memphis Power & Light Company and Memphis Natural Gas Company of the intrastate business done by Memphis Power & Light Company. On the contrary not only does the evidence without contradiction negative any such idea but all of the opinions of the court accept this. Although this is true, it is our submission that even if there had been joint control, it would we think, be fairly debatable as to whether this would justify the finding that Memphis Natural Gas Company was doing an intrastate business in Tennessee, so long as the separate corporate entities were preserved and were not part of an integrated system. Absent this, it seems clear that so far as the question of whether Memphis Natural Gas Company was engaged in intrastate business is concerned, it is entirely immaterial whether this was a profit sharing arrangement.

Mr. Justice Chambliss in his Dissenting Opinion accepted the illustration we brought to the attention of the court and added one of his own, saying:

> "I think the illustration suggested on the brief of counsel for the Natural Gas Company of the modernly common landlord and tenant lease contracts presents an apt analogy, the rental being based on the volume of business and incidental profits of the tenant. Here is a profit sharing compensation plan of fixing compensation, but the independence of the status of the parties is otherwise maintained, and the taxes, or other obligations of the parties, are not affected. Another simple illustration: A, a seller, in Dakota, contracts with B, a Tennessee buyer, to sell and ship wheat in such volume as the buyer may require through a given season. The price to be paid A is based on a fixed minimum sum per bushel, plus fifty percent of any excess realized by the buyer from his sales of the wheat: Does this profit sharing arrangement defeat the interstate commerce immunity of the interstate shipment? I think not."
>
> (R. 387.)

The fallacy in the assumption that profit sharing would have any such effect as Mr. Justice Fancher gave it can we believe be demonstrated. Suppose Memphis Power & Light Company had constructed a pipe line from Memphis, Tennessee, to the Monroe, Louisiana, gas fields, and that it had purchased gas from a producer in that field, a supposititious company, Louisiana Gas Producing Company. Natural gas was placed in this pipe line and transported to Memphis, there to be distributed by Memphis Power & Light Company. The contract between Memphis Power & Light Company and Louisiana Gas Producing Company as to the distribution of the so-called profits, we will assume, was substantially the same

as that between Memphis Power & Light Company and Memphis Natural Gas Company. Louisiana Gas Producing Company, however, had no pipe line in the State of Tennessee, had not qualified to do business in that state and had no connection with that state or any corporation which did do business within it, other than its contract with Memphis Power & Light Company. There was no stockholder who owned stock in both Memphis Power & Light Company and Louisiana Gas Producing Company. Under these circumstances it would, we submit, be absurd to argue that Louisiana Gas Producing Company was doing intrastate business in Tennessee. Yet if Mr. Special Justice Fancher was right in saying that Memphis Natural Gas Company was doing an intrastate business in Tennessee because of its contract with Memphis Power & Light Co., it would necessarily follow that Louisiana Gas Producing Co. in the illustration we have supposed would also be doing intrastate business in Tennessee.

So far as we have been able to find the only authority dealing with this question is furnished by the opinion of the Court of Appeals of New York in *People ex rel Pennsylvania Gas Company vs. Saxe, et al.*, 229 N. Y. 446, 128 N. E. 673, in which the court dealt with a similar arrangement between an interstate gas pipe line company and local gas distributing companies. In that case the amounts to be paid by the distributing companies to the pipe line company were based upon the gross receipts from distributors. The contracts were requirement contracts. The result was that the pipe line company which transported the gas in interstate commerce received from the distributors which distributed locally "from 80 to

86⅔ per cent of the gross receipts," the distributors "retaining the residue for themselves." Judge Cardozo (later Mr. Justice Cardozo of this Court) speaking for the New York Court, said:

> "We think the interstate character of the relator's (pipe line company's) business is untouched by these arrangements." (128 N. E. at 674.)

He further said that "the sale does not cease to be one in interstate commerce because the price is to be measured by the purchaser's receipts." (*Ibid.*)

Regardless of whether the contract between Memphis Power & Light Company and Memphis Natural Gas Company had the effect of a profit sharing or a quasi profit sharing arrangement, the result was not that found by Mr. Special Justice Fancher and this arrangement did not, as he held, prove that Memphis Natural Gas Company was doing intrastate business in the State of Tennessee. This being true the primary foundation upon which he places his conclusion is destroyed.

Contention That Tax May Be Sustained Even If Memphis Natural Gas Company Was Engaged Exclusively In Interstate Commerce.

In the Supreme Court of Tennessee it was insisted, in a belated reply brief filed on behalf of the Attorney General of Tennessee, that the decision in *McGoldrick vs. Berwind-White Coal Mining Co.*, 309 U. S. 33, was a departure from the well settled rule established by this Court that the privilege of doing interstate commerce cannot be taxed by means of an excise tax. The Supreme Court of Tennessee did not sanction this contention in any of the opinions delivered.

Without attempting to place the *Berwind-White case* exactly in its setting and without embarking upon a review of the decisions of the Court prior to that case—for we feel that such an attempt and such a review would unduly prolong the length of this brief and are unnecessary to a decision of this case—we point out that in our case there is present no one of the elements which were determinative in sustaining the tax in the Berwind-White case: there is here no tax upon a purchaser, no tax upon the transfer of title or possession, no tax that might be assimilated to a tax upon storage or use of property in the State of Tennessee. Here is a tax which amounts to one upon the privilege of engaging in interstate commerce, a tax implicitly condemned by the Berwind-White case itself.

Our submission is that the *Berwind-White case* is no extension of previous cases except that it holds that a sales tax may be imposed notwithstanding the fact that the sale was made pursuant to a prior contract to bring the goods from without to within the state. This distinction aside, it is entirely analogous to the use tax. The use tax, property tax or sales tax may be imposed upon property that formerly flowed in interstate commerce, after the end of the journey, and when it has become a mass of the property in the state.

This being the *sine qua non*, such taxes can not be imposed upon the vendor because his connection with the property within the taxing state is only that of a deliverer. The *Berwind-White case* thus viewed does not impinge upon the prior condemnation of excise taxes on

*See Powell—"New Light on Gross Receipts Taxes: The Berwind-White Case." 53 Harvard Law Review, p. 909.

the privilege of doing interstate commerce, or of taxes on interstate transportation.

This is a necessary conclusion because the right to engage in interstate commerce emanates from the federal power and not from the state power. The state possesses no authority therefore to impose a tax upon a privilege which it does not grant and cannot control but which flows entirely from the federal power.

CONCLUSION.

The conclusions we draw are these:

The taxing statute involved has been definitively construed by the Supreme Court of Tennessee as imposing a privilege tax. If it is applied, as it is sought to be applied by the taxing authorities of Tennessee, so as to reach the earnings of appellant, then it becomes a privilege tax upon the doing of interstate commerce. This is true because the entire earnings of appellant sought to be taxed were derived from interstate commerce. This commerce consisted during the tax years in question in the transportation and sale of natural gas. All other business of appellant, including the maintenance of an office in Tenneseee, was merely incidental to this business. There was no distribution of natural gas by the appellant within the State of Tennessee, and all its pipe lines in that state were main pipe lines. Appellant's business lost none of the characteristics of interstate commerce because of any corporate relationship with any corporation doing business within the State of Tennessee, because it was a distinct and separately controlled corporate entity. Nor did the contract between Memphis Natural Gas Company and Memphis Power & Light Company have this effect. The provision for adjust-

ments properly considered was a yardstick for rates. But even if considered as a profit sharing arrangement, the fact that Memphis Natural Gas Company may have received part of the profits of Memphis Power & Light Company does not in any sense mean that Memphis Natural Gas Company did an intrastate business within Tennessee. Properly viewed, therefore, the tax remains a typical privilege tax upon interstate commerce and thus seeks to tax a privilege which emanates from federal and not from state power and for this reason is to be condemned.

If these conclusions are approved by the Court, procedural questions become unimportant. The statute having been construed and applied to appellant's business is invalid under, and appellant has been deprived of a right, privilege and immunity guaranteed by, Article I, Sec. 8, Clause 3 of the Constitution of the United States. Therefore, whether the case is in this Court by appeal or whether the appeal be treated as a petition for certiorari, the result would be the same—the reversal of the Supreme Court of Tennessee and the remandment of the case for further proceedings not inconsistent with the views of this Court.

Respectfully submitted,

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APPENDIX "A."

Sections 1316-1318 of the Official Code of Tennessee of 1932 are as follows:

"Sec. 1316.—*Tax imposed.*—All corporations and joint stock associations organized under the laws of the State of Tennessee, other than those organized for general welfare and not for profit, and all corporations and joint stock associations organized under the laws of any other state or county for profit and doing business in Tennessee, shall, without exception, pay to the state comptroller annually an excise tax, in addition to all other taxes, equal to three per cent. of the net earnings for their preceding fiscal year of such corporations and joint stock associations, arising from business done wholly within the state, excluding earnings arising from interstate commerce. Tennessee insurance companies shall pay on net earnings proportioned to premiums on policies on persons and property in this state."

"Sec. 1317. *Credit for certain other taxes paid.*—Any corporation or joint stock association, paying the tax imposed, shall be entitled to a credit upon the tax imposed for the amount paid, in the preceding twelve months prior to July 1st of the year in which this tax becomes due, to the secretary of state under the terms of section 4136; insurance companies shall be entitled to a credit for all amounts so paid during the preceding twelve months under section 6 of the general revenue bill, and also under section 5716, and corporations or joint stock associations engaged in mercantile pursuits and paying the merchants' privilege tax to the State of Tennessee shall be entitled to a credit for the amount so paid during such preceding twelve months; and all other corporations and joint stock associations shall be entitled to a credit upon the tax herein imposed for any amount paid to the state for such preceding twelve months under any

general revenue bill, as a privilege tax, unless otherwise expressly provided in the statute imposing the privilege tax; provided, that the tax herein imposed is a state tax levied for state purposes only, and no county or municipality or taxing district shall have power to levy any like tax."

"Sec. 1318. *Due, when; penalty.*—The tax imposed shall be due and payable on July 1st of each succeeding year; and, if delinquent thirty days, shall be subject to a penalty of one per cent. per month, and, in addition, interest at the rate of six per cent. per annum from July 1st until paid."